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COMPULSORY LICENSING OF INTELLECTUAL PROPERTY IN EUROPEAN COMMUNITY ANTITRUST LAW

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Opinions expressed are purely personal.

After the Introductory Summary, this paper is in two parts. Part I summarises the principles of European antitrust law on compulsory licensing, in particular of intellectual property rights, as they have been generally understood. As there are so few European cases involving intellectual property rights, the underlying rules on essential facilities are explained here. It will be seen that these are broadly similar to US antitrust rules on essential facilities. This Part explains the reasons for the legal principles more fully than would normally be necessary, because some of them have been called in question in Europe.

Part II describes the decision of the European Commission in the IMS Health case which, if it is upheld by the European Community Courts, would substantially alter a number of the existing principles.

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Summary

Normally, it is pro-competitive to allow companies to keep for their own exclusive use assets which they have acquired or constructed. It is also, in general, pro-competitive to expect other companies to acquire or build corresponding assets for their own use, if they need them to compete.

However, under European Community antitrust law (as under US law) there is an exception to this general rule. Where a dominant company owns or controls something access to which is essential to enable its competitors to compete, it may be pro-competitive to oblige the company in question to give access to a competitor, if its refusal to do so has sufficiently serious effects on competition. This obligation arises only if the competitor cannot obtain the goods or services in question elsewhere and cannot build or invent them itself, and if the owner has no legitimate business justification for the refusal. The self-interest of the company in avoiding competition on the "downstream" market for which access is needed is <u>not</u> a justification.

In other words, the exception applies when <u>only</u> "downstream" competition is possible, and when <u>that</u> is possible only if access to the facility is given.

The basic rationale of this principle is that one competitor in a downstream market must not be able to get control over the only source of supply of an input which is essential in that market, and monopolise the market by shutting off supply to its rivals.

In European antitrust law, the following rules are fairly clear (some doubtful points are discussed below):

There is a duty under Article 82 of the European Community Treaty to contract on strictly non-discriminatory terms when all the following conditions are met:

(1) a company is dominant on the market for the supply of a product or service which is essential for competitors operating on a second market;

(2) there is no other actual or possible source of the essential product or service: competitors could not produce it themselves;

(3) objectively, competitors cannot operate on the second market without access to the product or service;

(4) the company is also dominant on the second market and a refusal to supply the product or service would confirm or strengthen its dominance there;

(5) there is scope for substantial competition on the second market, that is, it is not merely simple resale or distribution of products or services; and

(6) there is no objective justification for refusal to contract.

When a licence of an intellectual property right is asked for, the refusal to licence is unlawful only if the effect of a refusal would be exploitative or anti-competitive in some way not merely resulting from the refusal to licence itself. There must be some seriously undesirable element in the situation in addition to the natural result of the refusal to licence. This usually is, and perhaps must be, some specific loss caused to parties other than the competitors which may be excluded from the market by the intellectual property right.

Intellectual property rights: the principal situations summarised

A. If there is only one market, and the dominant enterprise uses its intellectual property right in that market, no compulsory licence could be ordered.

B. If there is only one market, and the dominant company does <u>not</u> use its IP right, no licence can be ordered under competition law (a compulsory licence might be possible under patent law).
There might be an exception if the dominant company had bought the IP right and then used it to suppress competition in order to protect an existing product of its own which was not protected by that particular IP right, at least if there was an unsatisfied demand for a new kind of product to which the unused IP right related.

C. If there are two markets, and the vertically integrated dominant company does not use its IP right in the downstream market, there is no duty to licence. This is because, if the dominant company is not in the downstream market, it has no duty to licence (Ladbroke judgment). If it is in the downstream market, but is not using the IP right, that shows that the IP right is not "essential". This conclusion treats the downstream market in the same way as the single market referred to at para B above. However, if the effect of the refusal to licence is that nobody can produce in the downstream market, this may be unlawful if the effect is to force buyers to buy the dominant company's product in the upstream market.

D. If there are two markets, and the dominant company uses the IP right in both (*e.g.* for a component or raw material, and for an end-product containing the component as an essential feature), there can be no compulsory licence, apparently no matter how great the value added is in the downstream market, except in specific cases:

(i) if by refusing the licence the dominant company is both monopolising the existing downstream market and preventing users getting a new kind of product for which there is an unsatisfied demand, then a licence may be ordered (*Magill* judgment); or

(ii) it seems reasonable to say that if the dominant company had previously given licences, and had let its licensees build up downstream activities on that basis, it could not then change its mind and terminate their licences, so that it could integrate forward without competition (cp. *Commercial Solvents* judgment, which however did not involve intellectual property rights). If the dominant company bought the IP right after the downstream market had grown up on the basis of licences granted by another company, the result would be the same; or

(iii) if the dominant company is refusing to licence and is charging prices which are so high as to be "unfair" and contrary to Article 82. (This would not be an antitrust violation under U.S. law). This might occur even if the dominant company had not got a 100% market share; or

(iv) if the dominant company is refusing to supply or licence the production of spare parts needed for the repair services market. This was said to be unlawful, in *Volvo v. Veng*.
If this is correct, it implies that monopolising a distinct second market may be unlawful even when intellectual property rights are used, and that the two grounds given in *Magill* are alternatives and not cumulative. Of course, people who need spare parts to be available for the repair of their equipment always suffer some loss if the supply of spare parts is not on a competitive basis, but in this situation, unlike *Magill*, there is no other loss caused specifically to end users. If this view expressed in *Volvo v. Veng* is correct, the second market would have to be distinct from the primary market. It would be sufficiently distinct if a compulsory licence could be ordered for that market without affecting the value of the dominant company's activities on the upstream market.

The alternative and probably better view is that when intellectual property rights are involved the requirements of *Magill* are cumulative, because a vertically integrated dominant company is entitled to use its IP right in any market to which the intellectual property right applies, but the right does not entitle it simultaneously to commit a distinct abuse against consumers. There is no clear basis in antitrust law for saying that an intellectual property right can be used to monopolise one kind of market but not another kind. If the requirements of *Magill* are <u>not</u> cumulative, it is hard to see what difference intellectual property rights would make, and the Court of Justice in *Magill* clearly thought that they do make a difference.

In all cases in which there may be a duty to grant a licence of an intellectual property right, refusal may be justified for specific reasons.

As already mentioned, in essential facility cases <u>not</u> involving intellectual property rights, two separate markets are always necessary.

PART I

Compulsory licensing in European antitrust law

The European Commission has stated its understanding of the general essential facility principle as follows:

> "An undertaking which occupies a dominant position in the provision of an essential facility and itself uses that facility (*i.e.* a facility or infrastructure, without access to which competitors cannot provide services to their customers), and which refuses other companies access to that facility without objective justification or grants access to competitors only on terms less favourable than those which it gives its own services, infringes Article 86 if the other conditions of that Article are met. An undertaking in a dominant position may not discriminate in favour of its own activities in a related market. The owner of an essential facility which uses its power in one market in order to protect or strengthen its position in another related market, in particular, by refusing to grant access to a competitor, or by granting access on less favourable terms than those of its own services, and thus imposing a competitive disadvantage on its competitor, infringes Article 86... [2]

There must always be <u>some</u> reason why a company which is in business to make money refuses to sell or licence something to someone who is willing to pay for it.

In European Community law, questions about the duty to contract with competitors arise in two kinds of cases:

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[2] This quotation is from the Commission's decision in *Sea Containers-Stena Sealink*, O.J. No L 15/8, 18 January, 1994.
For a summary of all the cases up to 1994 and a detailed discussion, see Temple Lang, Defining legitimate competition: companies' duties to supply competitors, and access to essential facilities, and Venit and Kallaugher, Essential facilities: a comparative approach, both in Hawk (ed.), 1994 Fordham Corporate Law Institute (1995), pp. 245-313 and pp. 315-344 respectively; Slot, General Report for the XIX FIDE Congress, Helsinki, 2000, on Community law including competition law affecting networks; Temple Lang, The principle of essential facilities and its consequences in European Community competition law (1996, Regulatory Policy Institute, Oxford); Temple Lang, The principle of essential facilities in European Community competition law – the position since Bronner, Journal of Network Industries (2000) 375-405.
The Telecommunications Access Notice (O.J. No. C 265/2, August 22 1998) is based on the same principle.

- when the company is in a dominant position in the upstream market (Article 82). The legal basis for a finding that Article 82 has been infringed may be either Article 82(b), which prohibits a dominant company from limiting the production, markets or technical development of its competitors[3], or Article 82(c) which prohibits discrimination; and
- when two or more companies join together to establish a production unit or other arrangement which they all use, and which gives them an advantage over their competitors (Article 81).

In European antitrust law, an "essential facility" may be a product such as a raw material, an intellectual property right, a service, information, infrastructure or access to a physical place such as a harbour or an airport[4]. It may also be a part of a telecommunications network. It is convenient to refer to all these as "facilities", although it is the Commission, not the Court of Justice which has used the phrase "essential facility". The principle now called "essential facilities" has been applied in Europe in a variety of different industries[5].

If a duty to give access or to licence arises, it is a duty to give access on non-discriminatory terms, that is, on terms corresponding to those given to the owner company's downstream

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3 Joined cases 40-48/73 *Suiker Unie* [1975] ECR 1663, pp. 1983, 2004: Commission decision British Telecommunications, O.J. No L 360/36, December 21 1982, para. 34: Notice on the application of the competition rules to access agreements in the telecommunications sector, O.J. No C 265/2. August 22, 1998, para. 88. Case 85/76 *Hoffmann La Roche* [1979] ECR 461 and Case 322/81 *Michelin* [1983] ECR 3461 should be regarded as based on Article 82(b). When the Court describes a particular type of conduct as contrary to Article 86, it often does not say which paragraph it is contrary to, either because it is often contrary to more than one, or because the list is not exhaustive: joined cases C-395/96P, *Compagnie Maritime Belge*, March 16, 2000, paras. 112 ff.

4 Advocate General Jacobs in case C-7/97 *Bronner v. Mediaset* [1998] ECR I-7791 at 7806-7807.

5 The phrase "essential facilities" was first used by the Commission in its decision in the *B&I - Sealink* case, 1992 5 CMLR 255, and in its decision in *Sea Containers - Stena Sealink* O.J. No L 15/8, 1994, quoted above. In those decisions however the Commission referred to a series of judgments of the European Court of Justice which are regarded as being based on the same or similar, legal principles beginning with joined Cases 6 and 7/73, *Commercial Solvents*, 1974 ECR 223. In addition to the recent judgments mentioned in the text, and to the Article 81 cases listed later, there have also been several other judgments and decisions which are based on the same principle: Case 311/84 *Telemarketing* [1985] ECR 3261: C-271/90 *Spain v. Commission (Telecommunications services)* [1992] ECR I-5833, para. 36
Port of Rødby, O.J. No L 55/52, 26 February, 1994.
ACI - Channel Tunnel O.J. No L 224/28, 30 August, 1994.
Night Services, O.J. No L 259/20, 7 October, 1994; annulled, Cases T-374/94, *European Night Services*, [1998] ECR II 3141.
Eurotunnel, O.J. No L 354/66, 31 December, 1994.
Ijsselcentrale, O.J. No L 28/32, 2 February, 1991: see 1992 ECR II 2417.
Irish Continental Group CCI Morlaix-Port of Roscoff, EC Commission, Twenty-fifth Competition Policy Report (1996), para. 43.
Port of Elsinore, May 1996, Commission press release, IP/96/456.
Cases C-241/91 P and C-242/91 *RTE and Independent Television* [1995] ECR I-743.
The Commission in its Guidelines on the application of EEC competition rules in the Telecommunication sector (O.J. No C 233/2, September 6 1991) said that refusal to provide reserved services (*i.e.* services for which a telecommunications company still has a monopoly) would be unlawful when it would make it impossible or difficult for competitors to provide non-reserved services. In this industry companies often need access to the networks of the main national telecom operators, and the essential facilities principle is therefore important.

operations or, if there are no such operations, on terms sufficient to comply with the requirements of Article 82(c). There is never a duty to provide access at a loss.

Compulsory licensing of intellectual property rights under European antitrust law – the cases

The question of compulsory licensing of intellectual property rights has arisen very seldom in European antitrust law.

The first case was *Salora v. IGR Stereo Television*[6]. German manufacturers of television transmission and receiving equipment had pooled their patents for a stereo television system, and their system was approved by the German authorities. They licensed themselves to produce TV sets, but refused to licence Salora, a small Finnish company, until after most viewers would have bought new sets. Salora complained, and the Commission ordered the German companies to grant Salora an immediate licence without quantity limits. No formal decision was adopted.

The first leading cases are *Volvo v. Veng* and *CICRA v. Renault*[7]. Car manufacturers owned the intellectual property (design) right for body parts for their cars. They refused to licence independent parts producers to imitate their designs. The Court of Justice ruled that the freedom of the owner of an intellectual property right to refuse to licence was the core subject matter of the exclusive right, and that the refusal in itself could not be an abuse of a dominant position which would be contrary to Article 82. The Court added that the refusal to licence could be an abuse only if there was some additional element, such as the refusal to supply spare parts to independent repairers, or stopping sales of spare parts for models still in widespread use, or charging excessive prices for the spare parts.

The next leading case was *Magill*[8], the television programs case. The television companies in Britain and Ireland refused to give lists of their next weeks' television programs to an independent weekly TV magazine called *Magill*, which wanted to publish all the programs on all the channels for each day. The Court of Justice confirmed that in the absence of "exceptional circumstances", the refusal to licence an intellectual property right is lawful. However, the television companies were ordered to give *Magill* the information, although they had argued that their program schedules were copyright. The Court gave three reasons for ordering disclosure:

- the information was indispensable for the production of a comprehensive TV program guide, a new type of product for which there was a clear and unsatisfied consumer demand;
- the TV companies, by refusing to provide essential information, were monopolising the separate market for TV program magazines; and
- there was no objective justification for the refusal.

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6 European Commission, Eleventh Competition Policy Report (1981) p. 63.

7 *Volvo v. Veng*, Case 238/87, [1988] ECR 6211; Case 53/87, *CICRA v. Renault*, [1988] ECR 6039.

8 Case C-241/91P, *RTE and ITP v. Commission*, [1995] ECR I 743.

Points to note are:

- what Magill magazine needed was the information. If it had been possible to provide the information without infringing the copyright in the program schedules, no copyright licence would have been needed;
- the Court did not say whether the two conditions for a compulsory license (preventing the sale of a new kind of product for which there was an unsatisfied demand, and monopolising a secondary market) were independent or cumulative[9];
- the copyrighted information was simply a list of programs and times, of no literary or artistic value.

In *Ladbroke*[10], it was claimed that French horse racecourses were unlawfully refusing to give a copyright licence to Ladbroke to transmit live pictures of French races in its betting shops in Belgium. The Court said the refusal was lawful, for two reasons. First, the French racecourses were not present on the separate Belgian market, so they could not be discriminating in favour of their own operations on that market. Second, Ladbroke was already on the Belgian market, and therefore live pictures could not be essential to do business on that market.

The most recent important judgment (although it is not concerned with intellectual property) is *Bronner*[11]. A newspaper publisher had the only home delivery service which covered the whole of Austria. It refused to provide delivery services for a competing newspaper. The Court said that the refusal would be unlawful only if it would eliminate all competition by the plaintiff, without objective justification, and if the service was indispensable because there was no actual or potential substitute. The Court said there were alternatives to home delivery, and nothing made it impossible to develop a competing home delivery system. The plaintiff had not shown that it would be uneconomic for competitors, acting jointly if necessary, to set up a second system on a scale similar to the existing system. The conclusion is not surprising, but the case is important because Advocate General Jacobs discussed "essential facilities" at length.

When is a facility "essential"?

The test of whether a facility is essential is whether normally efficient competitors could develop or obtain or get access to an alternative facility.

The test of indispensability is objective, and not based on the needs of the particular company requesting access. The Court in the *Bronner* judgment (paras. 44-46) said there were no obstacles making it impossible "for any other publisher of daily newspapers to establish, alone or in cooperation with other publishers, its own nation-wide home-delivery scheme". It would not be

9 See Case T-184/01R, *IMS Health v. Commission*, Order dated Oct. 26, 2001, para. 104. This question is considered below.

10 Case T-504/93, *Ladbroke,* 1997 ECR II 923: on appeal, case C-300/97P.

11 Case C-7/97, *Bronner v. Mediaprint* [1998] ECR I 7791; see also joined cases T-374/94 and others, *European Night Services*, [1998] ECR II 3141.

enough for the plaintiff to show that it is not economically viable for a newspaper with a small circulation: it would have to be shown that it was not economically viable for anyone to set up a distribution system of comparable size. These are substantive and objective tests.

The fact that the competitor seeking access is small, or inefficient for some reason, or especially vulnerable, or is particularly determined or well-financed, should not alter the legal duty to grant access, if any such duty arises in the circumstances. The dominant company could not assess the special needs of the competitor, but it can be expected to know what is objectively necessary in a market on which it is active. There is no duty to subsidise a competitor, and there is no duty to compensate for inefficiency or weakness.

This was the view taken, without explanation, by the Advocate General in *Bronner*[12]:

> "the test applied is an objective one, concerning competitors in general. Thus a particular competitor cannot plead that it is particularly vulnerable".

Since the test is objective, the question is not whether it is indispensable for one particular company's business, but for all competitors in its position.

A facility may be indispensable if no alternative can physically be created. But the question whether it is enough if it would be uneconomic to develop an alternative is more difficult. The Court in *Bronner* said:

- other "less advantageous" systems for distributing newspapers (post, sale at newsagents) were available (para. 43);
- no obstacle prevented one or more publishers launching a nation-wide home delivery scheme. In other words, competitors' initial lack of economies of scale does not make the facility "essential" (para.44);
- the competitor's small circulation does not make access to a nation-wide facility "essential" (para. 45);

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12 1998 ECR I, at p. 7809. See also pp. 7813-14. See also Case T-374/94 *European Night Services* [1998] ECR II-3141, para. 209 ("… no viable alternatives…").
The requirements that there should be only one facility and that the company must be dominant on the market for the supply of the facility are not necessarily equivalent. A company could be dominant even if there was a second facility, and there might be only one facility of a given kind even if there were some other kinds of facilities or other ways for customers to achieve the same result. There may be cases in which two jointly dominant companies each own a facility. See joined cases C-395/96P *Compagnie Maritime Belge*, judgment dated March 16, 2000, paras. 36-45. The Commission's Telecommunications Access Notice (O.J. No C 265/2, August 22, 1998, footnote 67) says access is compulsory if it is needed by all except exceptional competitors. On the questions of how a duty to supply may apply to jointly dominant companies, see Temple Lang, Some current problems of applying Article 82 EC, in Baudenbacher (ed.), Neueste Entwicklungen im Europäischen und Internationalen Kartellrecht, (Helbing & Lichtenhahn, 2000) 57-96, at 81-83; Temple Lang, Oligopolies and joint dominance in Community antitrust law, in Hawk (ed.), 2001 Fordham Corporate Law Institute (2002, forthcoming).

- to make the facility essential, one would have to prove "at the very least" that it was not economically viable to create a second delivery scheme with a comparable circulation (para 46.), *i.e.* with comparable economies of scale.

The Advocate General in *Bronner* said the principle applies:

- "for example where duplication of the facility is impossible or extremely difficult owing to physical, geographical or legal constraints or is highly undesirable for reasons of public policy. It is not sufficient that the undertaking's control over a facility should give it a competitive advantage. I do not rule out the possibility that the cost of duplicating a facility might alone constitute an insuperable barrier to entry… if the cost of duplicating the facility alone is the barrier to entry, it must be such as to deter any prudent undertaking from entering the market…."[13].

This seems to be substantially the same as the view that a facility is essential if without it there would be an insurmountable barrier to entry for competitors, or if without access competitors would be subject to a serious, permanent and inescapable handicap which would make their activities uneconomic (not merely less profitable)[14]. It would not make the facility "essential" to show merely that the dominant company had reached a threshold at which there were economies of scale.

Access to a facility is <u>not</u> essential if actual or potential downstream competitors, either alone or in combination, could build their own facility and would not permanently and inescapably be subject to a serious economic handicap by comparison with the existing facility. Competitors may need to "invent around" a patent. EU law obliges antitrust authorities to assess the objective impossibility of developing a second facility.

In other words, although applying an essential facility principle always involves an assessment of what competitors <u>could</u> do in the future, it does not involve assessing whether or not they <u>will</u> do it. If they <u>could</u> build a second facility on an economic basis, access will not be ordered. Competition on the basis of separate facilities is always preferred when it is possible.

In the case of an intellectual property right, competitors of course cannot develop their own identical rights. But the question is whether they could develop their own facility or intellectual property right which they could use instead of the right which they claim is essential. Usually they can: an intellectual property right does not necessarily give market power. Even a patent can be "invented around"[15].

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13 1998 ECR I, at pp. 7813-7814. The phrase "any prudent undertaking" implies a "rational investor" test.

14 Temple Lang, Defining legitimate competition: companies' duties to supply competitors, and access to essential facilities, in Hawk (ed.), 1994 Fordham Corporate Law Institute (1995), 245-313.

15 Under the European Council Regulation on Community Design, Reg. 6/2002, OJ No. L-3/1, January 5 2002 Article 8, there is no design right in features of a product which must be reproduced in their exact form and dimensions to allow the product to be mechanically connected to or placed in, around or against another product so that either product can function.

The need for two markets

In essential facility cases, there are two, related markets involved: the market for the supply of access to the facility in question, and the market for the goods or services for the production of which access is needed. A simple example is a car ferry which needs access to a harbour at each end of its proposed route. The market for supplying harbour services to car ferry companies is distinct from the market for car ferry services themselves, in which the buyers are owners and drivers of lorries and cars. The market for which access is needed is usually (but not necessarily) a "downstream" market, and it is convenient to refer to it as such. (Similar but not identical issues arise in connection with horizontally integrated companies producing two or more products which need to work together: these issues are not discussed in this paper).

The essential facility principle applies only when there are two distinct markets involved, and the product or service sold in one market (an "upstream" market) is a necessary input for the production of goods or services in the second ("downstream") market. There are strong reasons why the doctrine should be limited to two-market situations. The rationale for sharing essential facilities does not apply when there is only one market. The effect of applying the doctrine in single-market situations would be anti-competitive, and the possible benefits of doing so would be very small.

The basis for the essential facility principle is that if a facility supplied on one market is a truly essential input for the production of goods or services in a downstream market, then a competitor which has or obtains control of that facility would not be legitimately competing "on the merits" (that is, by offering better goods or lower prices) on the downstream market if it restricts access to the facility, or cuts off access to its competitors in that market. Such conduct harms competition and ultimately consumers.

It is only where there is a downstream market in which competition is absent or substantially lacking that the competition benefits of requiring access to private assets outweigh the damage to the incentive to invest, innovate, and develop the asset that would result from granting access (not only with regard to the owner of the facility to which access is requested, but to other developers and investors). The owner of the facility is allowed to profit from the market on which the facility is sold (otherwise there would be no incentive to create it), but it may not have the right to use it to monopolise a second, separate market.[16]

Every situation in which the essential facilities principle has been said to apply in EC law concerned two distinct markets, whether the input was a raw material,[17] access to a harbour,[18] or information about next week's television programs.[19]

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16 See Areeda & Hovenkamp, Antitrust Law (1996) Vol. III A ¶ 773.c.

17 Joint cases 6/73 and 7/73 *Instituto Chemioterapico Italiano S.p.A. and Commercial Solvents Corporation v. Commission* [1974] ECR 223 (market for a raw material and for derivatives of that material).

18 *Sea Containers v. Stena Sealink*, OJ 1994 L 15/8 (market for port services and for ferry services).

19 Joined cases C-241/91 P and C-242/91 P *Radio Telefis Eireann (RTE) and Independent Television Publications Ltd (ITP) v. Commission* [1995] ECR I-743 (market for TV listings and for weekly TV guides).

In order to establish whether two markets are necessary for the principle to apply, imagine a situation in which there is clearly only one market, where a vital element is essential in order to produce or sell in that market: in other words, the essential element is *not* something that could be bought by competitors in that market (since if it could, there would be two markets). If the essential element is necessary but has never been otherwise available, it must be something that has been developed by one or more competitors in the relevant market, and which is or has become necessary because it gives its owner an advantage (whether a better product or a cheaper process) which makes its owner's price or product unbeatable. In other words, in a single-market situation, whatever the details, something that is "necessary" to compete in that market can only be a competitive advantage, whether great or small.[20]

In assessing whether the essential facility principle could be applied to a competitive advantage in a one-market situation, the underlying principle must be that no one should be compelled to deal unless this significantly improves competition, since discouraging desirable behaviour would be anti-competitive.[21] Accordingly, if a competitive advantage, developed or invented by one competitor, was so unbeatable that companies which did not share it could not sell their products, it would be irrational if competition law, which is intended to promote the search for better products and cheaper processes, required the advantage to be shared.

Sharing an important competitive advantage on one market is an entirely different thing from ensuring access to an essential input which is, or was, available on a separate market. This distinction is fundamental: there is nothing pro-competitive in a competitor gaining exclusive control over the market for the supply of an input which is necessary for competition in a second related market. The essential facility principle applies in two-market situations because a competitor in the downstream market that gains control of a necessary input is *not* offering a better or a cheaper product in the downstream market, but only getting power to harm consumers in that market by shutting out its competitors.

It is inherently pro-competitive, on the other hand, to allow competitors to develop or invent their own competitive advantages in the markets in which they are operating. If competitors were required to share competitive advantages that are important enough, competition would be discouraged, not promoted.[22] A legitimate competitive advantage on a single market, even a decisive advantage, should therefore not be defined as an "essential facility."[23] This was explained by Advocate General Jacobs in *Bronner*:

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20 An element which is a "necessary" competitive advantage in a one-market situation may be inherently capable of being sold or marketed. However, if neither it nor any similar element has ever been marketed, there is no separate market. Most things could be sold or marketed if their owners wished to do so, but that does not make them into markets.

21 Areeda & Hovenkamp, Antitrust Law (1996) Vol. IIIA ¶ 773.a.

22 Areeda points out that "It is perfectly clear that the concept of monopolisation requires some element of impropriety; it has to be monopoly power coupled not with building the best mousetrap, but monopoly power coupled with some impropriety in its achievement or maintenance." Areeda, "Essential Facilities: an epithet in need of limiting principles," 58 Antitrust L. Jour., 841, at 846.

23 Turnbull, "Barriers to Entry, Article 86 EC and the Abuse of a Dominant Position: an economic critique of European Community competition law," [1996] 2 ECLR, 96, at 101.

> "In the long term it is generally pro-competitive and in the interest of consumers to allow a company to retain for its own use facilities which it has developed for the purpose of its business. For example, if access to a production, purchasing or distribution facility were allowed too easily there would be no incentive for a competitor to develop competing facilities. Thus while competition was increased in the short term it would be reduced in the long term. Moreover, the incentive for a dominant undertaking to invest in efficient facilities would be reduced if its competitors were, upon request, able to share the benefits. Thus the mere fact that by retaining a facility for its own use a dominant undertaking retains an advantage over a competitor cannot justify requiring access to it."[24]

It might be claimed that it was worthwhile to compel sharing of advantages, if it promoted competition between the companies sharing the most important advantages. This would be mistaken, for two reasons. First, sharing a competitive advantage would discourage competition if companies knew that, if they developed or invented competitive advantages which were valuable enough, they would have to share them with their competitors.[25] Second, when and if competitors did obtain the right to share the advantage, they would be sharing the same advantage with its owner and with a number of other competitors, all of which would have an equal right to it, on the same terms. Unless therefore the owner was required to subsidise its competitors by charging them a low rate of royalty, consumers would be unlikely to derive any significant benefit from it. Areeda in his article on essential facilities concluded that:

> "No one should be forced to deal unless doing so is likely substantially to improve competition in the marketplace by reducing price or by increasing output or innovation. Such an improvement is unlikely…when the plaintiff merely substitutes itself for the monopolist or shares the monopolist's gains."[26]

It is clear that two markets are a pre-requisite when intellectual property rights are said to be "essential facilities." This was the situation in the *Magill* case: the copyright arose incidentally out of broadcasting television programs, and copyright was claimed only as a reason for refusing to provide the program information which was necessary for a comprehensive TV viewers' magazine. The clearest way of explaining this is to say that if a licence could be given for an input in a separate market, and this can be done without affecting the right owner's statutory monopoly in the market to which the right primarily and directly relates, a compulsory licence may be ordered if the other requirements of the essential facilities principle are met. The "market to which the right primarily relates" would include all the markets for which the intellectual property right was developed or in which it would directly apply. The distinction seems to be between an intellectual property right insofar as it applies to all or the greater part of the markets to which it primarily relates, and a right insofar as it applies to one input in a market otherwise outside the scope of the IPR. This distinction can be applied only if the two markets are clearly distinct.

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24 Advocate General Jacobs in *Bronner, ibid.,* ¶ 57. See also in ¶ 65 of the same Opinion.

25 Korah, "*Patents and Antitrust*," [1997] IPQ No. 4 395, at 406. See also Bishop and Overd, Essential Facilities: the rising tide (1998) Eur. Competition L. Rev. 183.

26 Areeda, Essential facilities: an epithet on need of limiting principles, 58 Antitrust L.J. 841, at p. 852.

The examples given by the Court in the *Volvo* and *Renault* cases show that it would be unlawful to refuse to licence the manufacture of spare parts (one market) in order to force users to abandon their old products and buy new ones (the second market). They also suggest that it would be illegal to refuse to supply or to licence the production of spare parts which are a necessary input in the repair market, if the result was that the right owner could monopolise the repair and maintenance market.

Intellectual property, in contrast with most property, could be copied cheaply, easily, and rapidly. Since society considers the promotion of intellectual creation an important goal, intellectual property is protected by statutory monopoly rights, which provide a reward for initiative and investment in intellectual creation. Consequently, it is only when the intellectual property right holder uses the rights for a purpose which goes beyond their essential function, and seeks exclusivity in a market separate from that to which the intellectual property primarily relates, that anti-competitive conduct arises, and the essential facility doctrine can apply.

<u>The effect of the refusal on the downstream market</u>

The essential facilities principle applies only when the refusal has a substantial effect on competition in the downstream market. It seems that it applies only if a refusal to licence anyone would eliminate competition entirely on that market.

The practice of the European Commission is that, if the company is dominant not only in the market for the supply of access to the facility but also in the downstream market, a refusal to give access can be illegal even if it does not eliminate the plaintiff entirely, if the refusal has a sufficiently substantial effect on competition in the downstream market.

Several comments are useful:

- it would be impossible to justify the application of the essential facility principle if the refusal to supply had little effect on competition in the downstream market. Since antitrust law protects competition, not competitors, the principle should <u>not</u> apply merely because competition from <u>one</u> competitor is eliminated, if the downstream market is competitive without it. (However, in practice, a dominant company with spare capacity is not likely to refuse access unless the refusal benefits it in some way, which is likely to be by substantially reducing competition downstream.). The test therefore is whether refusal to supply <u>all</u> competitors, if such a refusal occurred, would have a substantial effect on competition;

- it would be unsatisfactory if a duty arose only if the refusal in question would eliminate or prevent <u>all</u> competition: a duopoly often provides little effective competition, especially when the two companies are using the same facility, the cost of which might represent a substantial proportion of their total costs;

- in all of the European antitrust cases so far, the refusal was considered to have a substantial effect on competition, the downstream market was uncompetitive, and the plaintiff was treated as a member of a class, so that a refusal to grant any licences would have meant that competition was eliminated;

- in intellectual property cases, if the "additional" element which makes the refusal to licence unlawful is that consumers are denied a new kind of product for which there is an unsatisfied demand, there is by definition no competition in the supply of that product (though that product need not constitute a separate market). If the "extra" element is that the dominant company is reserving to itself the separate downstream market "by excluding all competition on that market", by definition there is no competition in that market unless access is ordered;

- The test probably is whether there is a dominant position in the downstream market: in other words, the company must be dominant in both markets (or would be able to become so as a result of the refusal of any licences[27]). If so, a refusal to supply which creates or strengthens that position is unlawful because (if access to the facility is indispensable) the refusal limits the production of a competitor, contrary to Article 82(b). If the refusal does not prejudice consumers, because there is effective competition without it and the competitor which has been refused access was not planning to offer a new kind of product or service, Article 82(b) does not apply, though there may be a question of discrimination, under Article 82(c).

There must be inherent scope for competition in the downstream market

There is another pre-requisite for applying the essential facilities principle, which has not been brought out by the case-law so far. To justify imposing a duty to contract, there must be substantial scope for added-value competition in the downstream market for which access is required. This is important because it explains the generally accepted view that access to a product for mere distribution or re-sale, without substantial added-value services, can never be an essential facility.

Even where all the other requirements for the application of the essential facilities doctrine are met, it is only when the characteristics of the downstream market allow for substantial pro-competitive benefits for consumers that the doctrine should apply. To justify imposing a legal duty to contract, there must be substantial pro-competitive benefits for consumers to be

27 In theory, if a company was able to suppress competition on the downstream market by cutting off supplies, it would already be dominant even if it had not in fact behaved in that way. However, if there is competition on that market even though all competitors are using the same facility, in practice it is unlikely that the company controlling the facility would refuse access to one more if there was capacity available. The Commission's Telecommunications Access Notice (O.J. No C 265/2, August 22, 1998, para. 91) says that it is an abuse if the dominant company "fails to satisfy demand on an existing service or product market, blocks the emergence of a potential new service or product, or impedes competition on an existing or potential service or product market" (emphasis supplied).

obtained in the downstream market. This is not merely because of the transaction costs of imposing such a duty, and determining what the terms and conditions of access should be, although these transaction costs may be considerable.[28] It is also because, as explained, it is normally pro-competitive to allow even a dominant company to keep for its own use assets which it has acquired or developed.

Any potential benefits for competition can only be in the downstream market. In that market, if access to the essential facility is given on non-discriminatory terms, all the competitors to which access has been granted will be using the same facility at the same cost. The dominant company will also be using the same facility, although the net cost to it will be different, because it will have paid all the costs of developing or buying the facility, but will also receive royalties or other payment, however calculated, from its competitors. Competition will therefore be promoted only if there is inherently scope on that market for significant added-value services and genuine product differentiation between companies all using the same facility.

If, on the other hand, companies, all of which are using the same facility, can do little more than sell the result to consumers with substantially the same services and price (which will be governed by the payment which the competitors have to make to the owner of the facility), little has been achieved.[29] It is generally accepted that the essential facilities principle does not apply when the downstream market is merely resale: there is not enough scope for increasing competition to justify applying the principle. But this also means that in other situations where there is little scope for increasing competition, the principle should not apply either.

The essential facility principle should be used only if imposing a duty on the vertically-integrated dominant company to contract can achieve enough competitive benefits to outweigh the costs and risks involved[30]. The special rules relating to "price squeeze" cases, set out in the Commission's Notice on Access agreements in the Telecommunications sector, also implicitly assume that there is sufficient scope for downstream competition to justify antitrust intervention[31].

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28 Werder, "The Law and Economics of the Essential Facility Doctrine," 32 Saint Louis University L. Jour., 433, at 462-463.

29 An example of a regulatory obligation on a firm to share its inputs with a rival, which leaves scope for competition in added-value can be found in Article 6(1) of the EC Software Directive. Such a solution leaves a considerable amount of competition in added-value, as competitors are not given permission to replicate the original product. Instead, the Directive only ensures interoperability, thus allowing different applications that will differ in function and artistic design, while sharing the same interfaces (Council Directive 91/250/EEC).

30 Temple Lang, "The principle of essential facilities in European Community competition law – the position since Bronner," *ibid.*, 379-380.

31 How much scope there must be for packaging, ripening, added-value services or adding supplementary products to justify imposing a duty to give access to an essential facility does not need to be discussed here: the principle that there must be substantial scope, and the principle that mere resale or simple distribution is not enough, are clear.

The principle that the essential facilities doctrine should only apply where there is substantial scope for competition in added-value also prevents its application to one-market situations. If the essential facilities doctrine could apply in one-market situations, the result would be that, if a competitive advantage was important enough, it would have to be shared with a number of competitors (or with the number of competitors that the capacity of the supposed essential facility allows)[32]. As a result, all competitors which sell the same product would then sell it using the same advantage on the same terms, with little scope for competition in added-value. "Competition" means circumstances tending toward innovation, increased output, and reduced prices, not merely the existence of rivalry[33]. For example, there can be many kinds of ferry services using the same port (services to different destinations, using different vessels, transporting cars, cargo, or passengers, providing high speed or luxury services, *etc*.) Therefore, sharing the same port allows competition in added-value. But if a company developed an advantage relating to a particular service, and it was obliged to share it with all its competitors providing that service, there would be <u>less</u> competition in that service market. Merely changing the number of competitors on the market does not enhance competition[34]. In one-market situations it is particularly likely that compulsory sharing would reduce or eliminate the scope for competition, because that is essentially what it would be intended to do.

If it was seriously suggested that, when competition creates what seems to be an unbeatable competitive advantage, it should be shared compulsorily with competitors, even if no effective competition would result, the law would be more open than it has ever previously been to the criticism that it would be protecting competitors, not competition.

<u>When the dominant company is not present on the downstream market</u>

In most essential facilities cases, the dominant company is vertically integrated and has activities on the downstream market for which access to the facility is necessary. As already mentioned, the legal position when the dominant company is <u>not</u> present on the downstream market was considered in *Ladbroke*[35]. In this case, Ladbroke argued that the French horse racetrack owners had a duty under Article 82 to grant Ladbroke a copyright licence of the right to retransmit, to its betting shops in Belgium, live televised pictures of races in France. The Court of First Instance held that the relevant market was Belgium. The racetrack owners had granted no licences for Belgium, and were not present on the Belgian market. There was therefore no discrimination against Ladbroke and the French firms were not protecting their own downstream operations. The Court also distinguished the *Magill* judgment on the grounds that Ladbroke was already active in the Belgian market for which it claimed to need the pictures. Article 86 would apply only if the pictures were essential to betting shops in Belgium (which they plainly were not), or the refusal prevented a new product from being offered, despite a potential demand.

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32 If the facility was *software*, there would be no capacity limits, and the number of competitors which would be entitled to access would be unlimited.

33 Areeda & Hovenkamp, *ibid.*, ¶ 773.a.

34 Lipsky and Sidak, Essential Facilities, 51 Stanford L. Rev. (1999) 1187, at p. 1214.

35 Case T-504/93, 1997 ECR II 923: on appeal, case C-300/97P.

It seems therefore that if the dominant company is not present on the downstream market for which access to the facility is said to be essential, the essential facility principle does not apply. That is the view of the Commission, stated at the beginning of this paper. It is true at least in intellectual property cases such as Ladbroke.

Intellectual property rights and compulsory licensing under the essential facility principle

A company which owns a patent or other intellectual property right is not necessarily in a dominant position and does not necessarily have market power, because the product or process to which the right applies may not constitute a market separate from other products.

The basic principle in European antitrust law is that a dominant company which owns an intellectual property right is not obliged, merely because it is dominant, to licence the right. Mere refusal to grant a licence of an intellectual property right is not unlawful under Article 82. It is unlawful only if it is combined with some additional "abusive" element[36].

So a refusal by a dominant company to licence an intellectual property right may be contrary to Article 82 where:

- the refusal is combined with refusal by the dominant company both to produce and to allow others to produce, a product *e.g.*, a spare part for one of its old products, so that users will be forced to stop using that product and to buy its new product[37];
- a company owns the intellectual property right for a desirable new product and neither uses it nor licences it, to protect its existing products from competition. In the *Magill* case[38], television stations prevented the emergence of a single weekly magazine giving viewers details of all the main television stations' programmes. The Community Courts considered that although the single multi-station magazine would be in competition with the existing single-station magazines, it was a new and desirable type of product for which there was an obvious unsatisfied demand;
- the refusal leads to the dominant company unjustifiably refusing to supply companies who need parts for the repair services market[39]; or

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36 See Temple Lang, Abuse of Dominant positions in European Community law, present and future: some aspects, in Hawk (ed.), Fifth Annual Fordham Corporate Law Institute (1979) pp. 25-83. The phrase "abusive conduct" was used in Case C-241/91P *RTE and ITP* [1995] ECR I, at p. 823 but now seems less appropriate.

37 Under the "spare parts" clause in Article 8 of the EC Regulation 6/2002 on Community designs, OJ No. L-3/1, January 5, 2002, a Community design right cannot be obtained in features of the appearance of a product which are solely dictated by its technical function, or in features which must necessarily be reproduced in their exact form and dimensions to permit the product to be mechanically connected to another product to perform its function.

38 Case C-241/91P *RTE and ITP* [1995] ECR I-743.

39 Case 238/87 *Volvo v. Veng* [1988] ECR 6211: Case 53/87 *Cicra v. Renault* [1988] ECR 6039: Case 311/84 *Telemarketing v. CLT and IPB* [1985] ECR 3261: Case C-260/89 *ERT* (Greek television) [1991] ECR I-2927: Case T-65/89 *British Gypsum* [1993] ECR II-389, paras. 92-93: Case T-83/91 *Tetra Pak II*

- the refusal is combined with prices charged by the dominant company for its products which are so excessively high as to be "unfair" and prohibited by Article 82.

When the essential facility principle applies, it is usually because by refusing to licence the intellectual property right the dominant company is not merely using the right in the market for the product or service with which the right is primarily concerned, but is using it to obtain leverage or to protect itself from competition in another, distinct, market. In other words, Community law allows a dominant company to use intellectual property rights in the market for which the law primarily intends them to be used, but does not regard them as justifying cutting off an input which is essential on any other market, if that would otherwise be unlawful. This rule allows the dominant company to refuse to licence on the market with which the intellectual property right is primarily concerned. The more clearly distinct the two markets are, and the greater the restriction of competition on the second market which results from the refusal to supply, the stronger the argument for compulsory licensing. In the case of essential facilities, the remedy for a violation of Article 82 caused by refusal to licence intellectual property rights would be a compulsory licence of the rights involved, and not merely the termination of the "extra", abusive, behaviour. The crucial test usually is whether a compulsory license to allow the licensee to operate in the downstream market could be granted without affecting the right of the IPR owner to maintain its exclusive right in the distinct upstream market.

The grant of intellectual property rights involves a balancing of the public interest in free competition with providing an incentive for research and development and for creativity. Any application of the essential facilities doctrine should not be inconsistent with the exclusivity which is intended to preserve the incentive to create. If the essential facilities doctrine could be used to impose a duty to licence intellectual property rights to competitors on the market to which the rights primarily relate (if the firm is dominant, and the rights

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[1994] ECR II-755, at paras. 114-116: Cases C 241/91, 242/91 *RTE and ITV* [1995] ECR I-743. These cases show that in cases not involving intellectual property rights, using power in one market to strengthen the dominant company's position in a related market by lessening or eliminating competition in the second market is usually unlawful. The *RTE* case raised a considerable amount of controversy, in spite of the fact that the Commission, the Court of First Instance and the Court of Justice all agreed on the result.

This controversy was apparently due to two things:

(i) some critics seemed to be unaware of the Court's earlier case-law, and to object to the idea that competition law could ever limit the exercise of intellectual property rights; and

(ii) the second criticism was a more technical one, based on the facts of the case, and clearly expressed in a long, careful opinion of Advocate General Gulmann. This was based on the argument that although the broadcasting companies' dominant positions were in TV broadcasting, the copyright was in the lists of programmes, which was precisely what the Magill magazine wanted to obtain. The Courts brushed this argument aside, saying merely that the companies were using their dominant position in the TV market to monopolise a separate market for TV magazines, and implicitly treating the copyright in the programme list as incidental to the TV monopoly rather than copyright in an independent work.

It is worth mentioning that the IGR Stereo Television case, above, was treated as an Article 85 case by the Commission, and that the Commission was willing to order compulsory licensing by the patent pool if that had proved necessary.

create a sufficiently important competitive advantage), it would have the most profound implications, both for competition law and for intellectual property[40].

The Community Courts have said that if a dominant company was obliged to licence any important intellectual property right which it owned, it would be deprived of much of the value of the rights, since even generous royalties are not adequate compensation for the loss of the strategic freedom to use the rights in the way thought most profitable in the long term[41]. Compulsory licensing would convert intellectual property from an important competitive asset into a mere income-generating financial investment, and would deprive the owner of the power to use the rights for its own industrial or commercial needs. It would also, if the law frequently required compulsory licensing, deprive dominant or near-dominant companies of most of their incentives for obtaining intellectual property[42]. The value of intellectual property would be lessened and the purpose for which intellectual property was intended would be defeated[43].

If the essential facilities doctrine prohibited the refusal to licence valuable intellectual property rights in the market to which they directly relate, an abuse of a dominant position would be found in a large number of cases of refusals to licence intellectual property[44]. If a

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40 See concerning copyright, Case 158/86 *Warner Brothers Inc. and Metronome Video ApS v. Erik Viuff Christiansen* [1988] ECR 2605 ¶¶ 12-13; and concerning patents, Case 19/84 *Pharmon B.V. v. Hoechst AG* [1985] ECR 2281 ¶ 26.

41 In *Volvo*, the ECJ stated: "It follows that an obligation imposed upon the proprietor of a protected design to grant to third parties, even in return for a reasonable royalty, a licence for the supply of products incorporating the design would lead to the proprietor thereof being deprived of the substance of his exclusive right" (Case 238/87 *AB Volvo v. Erik Veng (UK) Ltd* [1988] ECR 6211, ¶ 8).

42 Cornish describes this as follows: "It can certainly be argued that this fencing off of intangible subject-matter fulfils an economic function equivalent to that of ownership of physical property, because otherwise the incentive to optimise the value of the information will be impaired or destroyed. Those who would be innovators will wait instead to be imitators and the dynamic processes which would have generated new ideas will disappear; in the end there will be little or nothing different to imitate." Cornish, *Intellectual Property: Patents, Copyright, Trade Marks and Allied Rights*, 4th ed., London 1999, 35.

43 The Commission has reached the same conclusion in a case concerning a request for compulsory licensing of intellectual property in the market to which it primarily relates: "it is highly doubtful whether one could impose an obligation upon a dominant firm (in an eventual EC bulk intermediate Hep B market), as a remedy to ensure the maintenance of effective competition in the national Hep B markets, to share its intellectual property rights with third parties to allow them to develop, produce and market the same products (*i.e.* multivalent containing the Hep B antigen) which the alleged dominant firm was also seeking to develop, produce and market" (Complaint by *Lederle-Praxis Biologicals*, XXIV Competition Report, point 353).

For completeness another possibility, not yet established in European antitrust law, should be mentioned. It corresponds essentially to the *Dell Computer* case, 121 F.T.C. 616, as determined by the FTC. If a dominant company knowingly allowed a standard to be developed which infringed its IPR, (in particular if it took an active part in developing the standard) and did not disclose the existence of the relevant IPR until after the standard had been adopted, it would probably be acting contrary to Art. 82 and the remedy might be a compulsory licence of the relevant IPR to users of the standard. Such conduct would also be contrary to *e.g.* the European Telecommunication Standards Institute (ETSI) rules on IPRs: European Commission, 25th Competition Policy Report (1995) pp. 131-132.

44 Venit and Kallaugher, "Essential Facilities: a comparative law approach*,"* in Hawk (ed.), Fordham Corporate Law Institute, International Antitrust Law & Policy (1995), 337.

competitor could claim that an intellectual property right is an essential facility merely because it involves a clear competitive advantage, no owner of intellectual property rights could be sure of enforcing valuable rights, since any intellectual property might have that effect[45]. Moreover, the essential facilities doctrine, if applied in a single market situation, would weaken intellectual property rights precisely when this result is least defensible: the more an invention was unique, valuable, and difficult to duplicate, the greater would be the obligation to share it[46].

The situation is materially different where the owner of intellectual property rights in one market (the "upstream" market in the terminology used here) is able to use these rights to foreclose competition in another market. In such case, the dominant company is not merely using the essence of the intellectual property rights ("the essential function" in the language of the Court of First Instance in *Magill*[47]), namely the power to refuse to licence the rights in the market to which they relate. There is therefore an anticompetitive element distinct from the mere refusal to licence, and in *Volvo v. Veng* it was said that this additional element makes it legitimate (provided that the other conditions for applying the essential facility principle are met) to say that the appropriate remedy for the monopolisation of the downstream market is a compulsory licence of the intellectual property rights for the purposes of the downstream market[48]. Even if there has been additional conduct constituting the abuse which is contrary to Article 82, the remedy is *not* compulsory licensing in the market to which the rights primarily relate, but <u>only</u> a compulsory licence sufficient to prevent the dominant company from monopolising the <u>second</u> market. The dominant company remains free to refuse to licence its competitors on the upstream market.

If this statement in *Volvo v. Veng* is correct, it would follow that in *Magill* it would have been unlawful for the broadcasting companies to monopolise the weekly TV magazine market, even if they had not also been depriving consumers of a new kind of product for which there was an unsatisfied demand. In other words, the findings in *Magill* should be regarded as alternatives, and not cumulative. This would make necessary criteria for distinguishing separate downstream markets. However, the better view seems to be that the *Magill* findings are cumulative, since it is hard to see why antitrust law should allow the use of an intellectual property right to monopolise one kind of market and not another kind.

In *Volvo* and *Renault* the Court of Justice also mentioned another situation in which there may be an abuse, contrary to Article 82, because the dominant company had charged excessively high prices, and this abuse was linked to a refusal to licence intellectual property rights[49]. This situation is also consistent with the principle that a refusal to licence by itself

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45 Reasoning along these lines brought the court to reject an essential facilities claim in the U.K. Case CH 1997 P No 4100 and CH 1997 P No 4101 *Philips Electronics NV v. Ingman Limited (t/a Diskexpress*), May 13, 1998.

46 Lipsky and Sidak, "Essential Facilities," 51 Stanford L. Rev. (1999), 1187, at 1219. This leads the authors to conclude that essential facilities principles should not apply to intellectual property under US law.

47 Case T-69/89 *Radio Telefis Eireann v. Commission* [1991] ECR II-485, ¶ 71.

48 Temple Lang, "Defining Legitimate Competition: companies' duties to supply competitors and access to essential facilities," *ibid.*, 519.

49 *Volvo, ibid.*

cannot be an abuse, and that if there is a violation of Article 82, it lies in another, separate, abusive element. But this situation is the only one envisaged by the Community Courts in which the refusal to licence and the separate abuse would concern the same market. There are two explanations. The first is that in the case of excessive pricing, the violation of EC antitrust law is not the refusal to licence, but the excessive price, and the compulsory licence, if one is appropriate, is simply the most effective remedy. (In all other cases it is the refusal to licence which is the essence of the violation, even though refusal to licence an IPR cannot be a violation unless there is some additional element). The second explanation is that this is the only one of the hypothetical abuses in *Volvo and Renault* which is an "exploitative" abuse as distinct from an "anti-competitive" or "exclusionary" abuse[50]. The abuse of excessive pricing (which is not a violation of Section 2 of the Sherman Act) is committed against buyers, while anti-competitive abuses are committed, in effect, against competition and against competitors. In all cases in which the additional abuse is an anti-competitive one, the compulsory licence would concern a different market or at least a different category of goods from that to which the intellectual property rights primarily relate[51].

Justifications for denying access to essential facilities

The basic principle is that if a reasonable owner of the facility who had no interest in any downstream operation would have a substantial interest, acting rationally, for refusing access, the owner is entitled to do so.

So an owner may refuse access:

1) if giving access to the applicant would reduce the efficiency of the downstream users or licensees, including ultimate users, or

2) would reduce the efficiency or value of the facility or intellectual property right, or

3) would cause the facility or IPR to be used uneconomically, or at a lower price than the owner could otherwise obtain[52], or for a purpose wholly different from its current use;

4) would interfere with the improvement, expansion or development of the facility or IPR, or

50 In *Magill*, depriving viewers of a comprehensive weekly TV magazine, and thereby obliging them to buy several single-station magazines, was also exploitative.

51 If excessive prices contrary to Article 82(a) are charged for patented goods, a compulsory licence of the patent would be a market-based remedy, more effective, and easier to apply than continuing price supervision by a competition authority.

52 Except that the owner of the facility cannot insist on obtaining monopoly profits, or on enabling downstream users to obtain them.

5) would interfere with technical or safety or efficiency standards, *e.g.* by causing undue congestion, or by causing compatibility problems in the operation of software.

6) if the owner can show genuine and objective advantages of vertical (or horizontal) integration which could not be achieved by reasonably close cooperation with an independent company, that might justify refusal. The advantages would have to be substantial enough to outweigh the anti-competitive effects of refusal. Normally, the dominant company should put its competitors out of the market by competing on the merits, not by refusing access. A dominant company cannot justify a refusal to give access by claiming to be more efficient than its competitors: it is not well-placed to judge, a dominant company should not be allowed to decide the lawfulness of its own conduct, and the competitor, when put under pressure, might be able to become more efficient.

7) if the company seeking access was not creditworthy or has not got the professional and technical skills needed to share the facility.

8) if there is no spare capacity available, that may be (but is not necessarily) a justification. This is not an issue likely to arise with IPRs. In general the owner's obligation is to provide access on a non-discriminatory basis up to the optimum or maximum number of users, determined objectively. So it can refuse access to a user who would be "one too many". Also, the current capacity of the facility might have been intended as a constraint on competition in the downstream market[53] and the new entrant might be willing to pay to create extra capacity.

Intellectual property rights are <u>not</u> always a sufficient reason for refusing access but, as explained above, might be a sufficient reason.

The owner may be able to justify differential treatment to encourage new entrants by giving them low initial charges, or to oblige new entrants to make an appropriate contribution to capital costs, or to deal with particular categories of users.

In times of shortage, traditional customers and those with long-term contracts may be given a preference. Long term agreements may be a justification for refusing access, provided that they are not themselves unduly restrictive (by being of too great duration, taking into account the investment being made on the basis of the agreement by either or both parties, and whether this expenditure led to an increase in the capacity of the facility). So if the existing facility is fully used, a new entrant may have to wait until one of the existing contracts comes to an end.

If a user has financed some extra capacity, it is entitled to <u>some</u> priority. It is easier to defend such a priority if there has been an open invitation to tender at the time when finance was provided.

[53] Lipsky and Sidak, Essential Facilities, 51 Stanford Law Review (1999), 1187-1248, at pp. 1221-1222.

Where the owner of the facility needs to justify an otherwise unlawful refusal to licence, it may be necessary to balance the anticompetitive effects of the refusal against the suggested justification.

Multicompany situations

In Europe, the essential facilities principle is usually thought of in connection with monopolies. However, similar economic issues arise when two or more companies make arrangements to establish joint or reciprocal operations[54]. In these circumstances third parties may find that they cannot do business with the companies involved, or that they can do so only on less favourable terms than those obtained by the parties or by the joint venture. The question then arises whether the parties should be entitled to refuse to contract with third parties, or entitled to give third parties less favourable terms than they give to one another.

In a variety of different situations involving joint operations, the parties may be prohibited from discriminating in favour of the joint venture (or of one another) if discrimination would impose a significant handicap on competitors[55].

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54 See Temple Lang, International joint ventures under Community law, in Hawk (ed.), 1999 Fordham Corporate Law Institute (2000).

55 In the following cases, among others, the Commission imposed or took note of duties or accepted undertakings not to discriminate against non-parties:
IGR Stereo Television-Salora, EC Eleventh Competition Policy Report (1981) p 63; *Amadeus-Sabre*, see for the text Temple Lang, Air Transport in the EEC-Community Antitrust Law Aspects, in Hawk (ed.), 1991 Fordham Corporate Law Institute (1992), ch. 15 pp. 317-322.
DHL International, EC Commission Twenty-first Report on Competition Policy (1991), para. 88.
Eirpage, O.J. No L 306/22, 7 November 1991, para. 20.
Infonet, Twenty-second Report on Competition Policy (1993), p. 416.
EBU-Eurovision, O.J. No L 179/23, 22 July 1993, Art. 2.
BT-MCI, O.J. No L 223/36, 27 August 1994, para. 57
ACI, O.J. No L 224/28, 30 August 1994, Art. 2.
European Night Services, O.J. No L 259/20, 4 October 1994, Art. 2.
Gas Interconnector, Commission's Twenty-fifth Competition Policy Report (1996), para. 82.
Atlas-Phoenix-Global One, O.J. No L 239/23, L 235/57, 1996.
Unisource-Uniworld, O.J. No L 318/1 and L 318/24, 1997.
British Interactive Broadcasting, O.J. No L 312/1, 1999.
NC/Canal+/CDPQ/Bank America, M.1327, decision dated Dec. 3, 1998.
Allied Signal/Honeywell, M.1601, OJ No. L-152/1, June 7, 2001, para. 128.
Air Liquide/BOC, M.1630, decision dated January 18, 2000, para. 296.
Vivendi/Canal+/Seagram, M.2050, decision dated Oct. 13, 2000.
Vodafone Airtouch/Mannesmann, M.1795, decision dated April 12, 2000, paras. 58-59.
BSkyB/Kirch PayTV, JV.37, March 21, 2000, paras. 92-94.
In Nordic Satellite Distribution, O.J. No L 53/20, 2nd March 1996 the parties were willing to give an undertaking not to discriminate, but the agreement was ultimately prohibited. (Similar undertakings were also offered in *MSG Media Service*, O.J. No L 364/1, 31st December 1994 and in *Bertelsmann/Kirsch/Premiere* and *Deutsche Telekom/BetaResearch*, O.J. No L 53/1 and L 53/31, 1999.) This is because a merger which creates a dominant position contrary to Reg. 4064/89 cannot be made lawful merely by assurances that it will not abuse its dominance.

Although the underlying economic problems under Article 81 are similar to those in cases under Article 82, there are certain obvious legal differences:

- the Articles are differently worded, so the legal basis appears to be different;
- the crucial criteria seem to be different (under Article 81(3), it is usually the fourth requirement, summarised below);
- in Article 81 cases, the parties are usually giving themselves the benefit of the facility, so it is the discrimination principle which applies and not necessarily the duty to contract; and
- in Article 81 cases, the standard of comparison for the duty to give non-discriminatory access is available: it is what the parties themselves have obtained.

Any multicompany or joint venture arrangement which substantially restricts competition needs to comply with the four requirements of Art. 81(3) EC. In the case of arrangements involving control of an important facility, the crucial legal requirement is usually the fourth, which says that restrictive agreements must not enable the parties to eliminate competition in respect of a substantial part of the goods or services concerned. So joint ventures and similar arrangements are usually required to grant competitors access on non-discriminatory terms when the parties would otherwise be in a position to eliminate competition in respect of a "substantial" part of the products concerned, either by refusing to supply competitors or by supplying them only on substantially less favourable terms. This is a lower threshold than when the essential facility principle applies to a single dominant company, because a single dominant company normally has no duty to supply if there is even one alternative source available.

Whether such a duty should be imposed depends, among other things, on the combined market shares of the parents and the joint venture in both the relevant markets, on any other advantages which they have (especially if they might amount to dominance), on the extent of the disadvantage imposed on competitors (the extent of foreclosure), the extent to which competitors need to cooperate with the parties and are thus dependent on satisfactory cooperation from them, what alternatives, if any, are available to competitors, whether membership in the arrangement is freely open to competitors, and on any justification which may be available for denying the benefit of the arrangement to non-parties, or for modifying the terms offered to them. A duty may be imposed even if the parties are not controlling a facility which is so essential that non-parties could not do business without it.

Access on non-discriminatory terms may of course involve the competitor complying with all reasonable criteria or requirements or making an appropriate contribution to the joint operations: there is never a duty to provide better terms to non-parties than to parties. It is also relevant to know whether the parties could share with competitors the same services on the same terms without lessening the benefits of the arrangement to themselves (apart of course from the fact that they would no longer have that particular advantage over their competitor). It is always relevant to ask whether the benefits of the arrangements are obtained primarily by the parties, or whether benefits are obtained directly by consumers as well, as *e.g.* in the case of airlines computerised reservation systems and interlining arrangements, banks' cheque clearing facilities, and telephone companies' reciprocal use of their networks. The duty to grant access arises only if without it the market would not be competitive, *e.g.*, there would be too few companies which did not suffer from a significant handicap as a result of being denied access to the joint arrangement. It is also relevant how far the joint arrangement reduces competition between the parties to it, and how far (if at all) it would be possible, satisfactory and pro-competitive for competitors not involved in the joint operation to set up a rival one of their own which would do substantially the same things in the same geographical area, in competition with the first joint operation.

In deciding whether there should be a duty to grant access, different considerations arise in different kinds of multicompany situations:

- reciprocal cooperation between competitors may be essential to carry out the operations in question, as in the case of banks' cheque clearing systems and airlines' interlining arrangements. Such arrangements have network effects (they are better the more participants there are). If all technically necessary requirements are fulfilled, exclusion would be hard to justify, as it would create a category of second-class competitors;
- where a joint operation is needed to provide a service for all the participants, which could not be provided otherwise because of *e.g.* insufficient economies of scale. This raises issues about the capacity of the joint operation, and whether another group of competitors could jointly set up an economically efficient rival. Because an arrangement which reduces costs is pro-competitive and does not impose any handicap on competitors, or deny them the possibility of cutting costs in the same or any other way, there is normally no duty to give access to competitors;
- cases in which an essential facility has been developed by one company primarily for its own use, and ownership is later shared with other companies using it. These cases are often a subset of the situations in which the joint venture owning the essential facility is in a dominant position, and the fact that the users are also shareholders does not significantly alter the legal or economic position (except of course that it creates both the temptation and the opportunity to discriminate);
- cases in which a consortium of users or buyers have joined together to get control of an important source of supply, from which they had previously bought but which none of them had previously owned, controlled or developed. In such cases the right of third parties to get access is likely to be clear, as otherwise the arrangement would be similar to a collective boycott;
- when competitors have set up a pool of patents, in particular if the patents are complementary, so that the combination cannot be duplicated or invented around, and in particular if the patents constitute a de facto standard, they are obliged to licence all the patents needed by non-parties to compete[21)];
- in a network industry, if a consortium sets up a joint venture which will use all of the facilities owned by the parties in different geographical areas, and it would be difficult or impossible for any other competitor or consortium to set up a similar network of facilities in all the same areas. Such a situation arises in telecommunications, and in rail transport. In such circumstances competitors would normally have a right of access under Art. 81, quite apart from any sector

[56] *IGR Stereo Television-Salora*, European Commission Eleventh Competition Policy Report (1981) p 63: Case C-241/91P *RTE and ITP* [1995] ECR I-743.

specific measures, at least if the areas in the Community to which the network in question controls access are "substantial".

To summarise, therefore, when competitors together create, own or operate an important facility access to which is essential for the competitiveness of the market and of non-participant competitors, and where admission of non-participants is compatible with the legitimate purposes of the joint arrangement, the participants are likely to be obliged to grant access to competitors on non-discriminatory terms, under Article 81.

It will be seen that in multicompany and joint venture cases almost all the same kinds of problems arise as in the case of single-firm ownership of an essential facility. It may be necessary to ensure that access is available to other competitors, to enable them to do business without a serious handicap. On the other hand, it may be significantly pro-competitive to allow the parties to keep for themselves the benefits which their joint investment or their joint ingenuity have obtained for them. The important difference concerns transaction costs: in a multicompany situation there are already agreements between the companies involved, and it is therefore not usually difficult to determine what non-discriminatory terms for a competitor would mean. The transaction costs of a duty to contract are much less in Article 81 cases. This makes the duty more likely to arise.

The question of payment

Apart from the need to allow for different degrees of risk, to say that payment must be on a non-discriminatory basis is normally an adequate and self-explanatory approach when a standard of comparison is available. Even in the case of a vertically integrated dominant company without separately incorporated companies, it should be possible in theory (although it might be difficult in practice) by cost accounting to calculate an arms'-length transfer price between the upstream and the downstream markets. However, this would be impossible if there is no distinct upstream and downstream markets. Also, the Commission has never dealt with the question of how to decide what rate of payment is fair and reasonable when there is no standard of comparison because no licensor has ever given a comparable licence; in *Magill* the Commission did not try to decide what rate of royalty would be appropriate, and simply ordered the parties to agree on a reasonable rate.

PART II

Since the judgment of the Court of Justice in the *Magill* TV programs case in 1995, the European antitrust law principles were generally regarded as well-settled and clear in most respects. However, in 2001 the Commission adopted a decision in *IMS Health*, which put a number of these principles into question[57].

[57] OJ No. L-59/18, February 28, 2002.

There are several reasons why it is difficult to write about this decision. It is at present *sub judice*, on appeal in the Court of First Instance[58]. Several issues which are essentially the same as those in the Court of First Instance have been raised in a case referred by the German courts to the Court of Justice, which is also *sub judice*[59]. The decision is an interim measures (interlocutory) decision, and therefore not as fully considered and explained as a final decision normally would be. The Commission seems to have changed its legal position, and it is not clear that it has understood or accepted the implications of what it seems to be saying. Last, my law firm, Cleary Gottlieb Steen and Hamilton, is representing IMS Health in both Community Courts.

IMS Health provides pharmaceutical companies with information on sales of pharmaceutical products in Germany, among other countries. This information is used, in particular, as the basis for paying sales representatives. Since these representatives talk to doctors and not to patients or pharmacists, and since patients who get prescriptions from doctors may buy the prescribed drugs from pharmacies where they live or work and not from pharmacies in the neighbourhood of the doctor, collecting and presenting the information in a way that best allows the pharmaceutical companies to measure the effectiveness of their sales representatives is complex and difficult. European data privacy laws do not permit sales data to be presented in a way which would allow readers to identify the sales of any individual pharmacist. IMS Health solved this problem by producing a map of Germany divided into areas, called "bricks", drawn so as to group together in each area as far as possible a full range of specialist doctors and the pharmacists to whom their patients are likely to go, to have prescriptions made up. IMS Health then collects sales data from wholesalers which sell to the pharmacists, and supplies the data to pharmaceutical companies on the basis of each area or "brick". These bricks are then used as the basis of the representatives' sales territories.

When it appeared that competitors of IMS Health were using the brick structure which IMS had developed, (in which Germany was divided into 1860 bricks), IMS sued for copyright infringement, and the German courts accepted that the map of 1860 bricks was copyright. The competitors complained to the European Commission, arguing that, in effect, the use of IMS's brick structure was essential for them to supply sales information to pharmaceutical companies. The Commission, by an interim measures decision in July 2001, ordered IMS to grant a copyright licence to its two competitors. IMS appealed against this decision, and in October 2001 the decision was suspended by Order of the President of the Court of First Instance[60].

This Order says that a judge should "normally treat with circumspection a Commission decision imposing, by way of interim measures … an obligation … to licence the use of [an] intellectual property right … The Commission's provisional conclusion that the prevention of the emergence of a new product or service for which there is a potential consumer demand is not an indispensable part of the notion of "exceptional circumstances" developed by the

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58 Case T-184/01, *IMS Health v. Commission*.

59 Case C-418/01, *IMS Health v. NDC Health*.

60 Case T-184/01R, Order dated October 26, 2001. See Schwarze, Der Schutz des geistigen Eigentums im europäischen Weltbewerbsrecht, Europäische Zeitschrift für Wirtschaftsrecht 3/2002, 75-81.

Court of Justice in *Magill* constitutes, at first sight, an extensive interpretation of that notion …" The Order added that the requirements in *Magill* may be cumulative.

Also in 2001, the German courts, which had concluded that European antitrust law did not entitle the competitors to copyright licences or prevent IMS from claiming its rights under copyright law, referred to the Court of Justice several questions intended to resolve the conflict between the judgments of the German courts and the decision adopted by the Commission.

In April 2002 the President of the European Court of Justice dismissed an appeal against the Order of October 2001, substantially confirming all the findings made in the earlier Order.

On the legal issues, the Commission now emphasises that pharmaceutical companies helped IMS Health to develop its 1860 structure (though they do not own the copyright jointly and they never agreed to use it or to treat it as an industry standard) and that they have good reasons for not wanting to switch from the 1860 structure. Even on this basis, the Commission's decision against IMS Health goes further than the *Magill* television programs case in several respects[61]:

1. The Commission says that a licence of the IMS Health copyright is an "essential facility" merely because pharmaceutical companies do not want to use any brick structure except the IMS 1860 structure, although competitors can develop their own "brick" structures or maps.
2. Apart from the refusal to licence the copyright, there is no additional element or conduct by IMS which could be unlawful.
3. The Commission says that the "exceptional circumstance" which justifies a compulsory licence is that, since customers want to use only the IMS copyright, if there is no compulsory licence, there is no competition.
4. The Commission says that there is no need for two separate markets in compulsory licence or essential facility cases: it is enough if there are separate stages of production, and that any distinct input, or apparently any intellectual property right, could be an essential facility if it is valuable enough, even if it is of a kind which has never previously been marketed or licensed by any company.
5. The Commission says that it is enough if the proposed licensees would offer substantially the same product or service as the intellectual property owner, and that they do not need to offer a new kind of product or service for which there is an unsatisfied demand.

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61 Other differences include the facts that in *Magill*, the information about next week's programs was owned by the TV companies, in *IMS Health* the sales data was freely available from wholesalers; in *Magill*, nobody could produce a substitute for the program list, while in IMS Health the plaintiff had produced their own brick structures; in *Magill,* the TV companies had discriminated, because they had given program information to daily newspapers and foreign magazines, but IMS Health had never licensed its brick structure to a competitor except when it sold a business; in *Magill*, the TV stations could make a profit from supplying valuable information while still allowing a comprehensive magazine to start up; licensing in *Magill* did not affect the core of the TV companies' copyright, they still needed to produce program listings; the plaintiff in *Magill* had not infringed copyright rights; *Magill* was a final decision, not an interim measures decision.

Taken together these principles[62] would apparently imply that:

- customer preferences, if strong enough, can make a competitive advantage into an essential facility which the dominant owner must share with rivals;
- a monopoly or near-monopoly position can be made the subject of compulsory intellectual property licensing, even if no abuse has been committed;
- a compulsory licence can be ordered to oblige a dominant company to share its principal competitive advantage with its competitors; and
- a refusal to licence an intellectual property right, without more, is prohibited by European antitrust law if the right is so valuable that it leads to a monopoly or near-monopoly.

In short, there are a number of very surprising and controversial features of the Commission's decision. It seems reasonable to say that it seems likely that it will be struck down.

The IMS Health decision shows how easily the principle of compulsory licensing of intellectual property rights can be applied in a way which would seriously discourage innovation and competition, even when applied by an antitrust authority previously regarded as having sound judgment.

If the Community Courts in due course were to uphold the validity of the Commission's decision, whatever the precise grounds might be on which the Courts would base such a judgment, European antitrust law would have gone much further than the *Magill* television programs case in the direction of compulsory licensing and towards reducing the value of intellectual property rights.

[62] The *IMS Health* decision is also open to the objection that it would be impossible to determine a satisfactory rate of royalty for the licence envisaged by the Commission, but this question was not dealt with in the decision.